

Stephenson, Gracik & Co., P.C.

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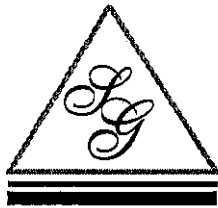
VILLAGE OF STERLING
ARENAC COUNTY, MICHIGAN

AUDITORS' REPORT
YEAR ENDED MARCH 31, 2008

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AUDITORS' REPORT

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August 27, 2008

Independent Auditors' Report

Members of the Village Council
Village of Sterling
Arenac County, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the Village of Sterling, Arenac County, Michigan, as of and for the year ended March 31, 2008, which collectively comprise the Village's basic financial statements, as listed in the index. These financial statements are the responsibility of the Village of Sterling's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and each major fund of the Village of Sterling, Arenac County, Michigan, as of March 31, 2008, and the respective changes in financial position, and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2, the Village of Sterling has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, as of March 31, 2008.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 27, 2008, on our consideration of the Village of Sterling's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Stephenson, Gracik & Co., P.C.

VILLAGE OF STERLING
P.O. Box 165
STERLING, MI 48659

MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis of the Village of Sterling's (the Village) financial performance provides an overview of the Village's financial activities for the year ended March 31, 2008. The intent of this discussion and analysis is to look at the Village's financial performance as a whole. The discussion focuses on the Village's primary government.

Financial Highlights

- The Village's assets exceeded its liabilities by \$1,534,136.
- The Village's total net assets increased by \$51,561.
- The Village's governmental funds reported a combined ending fund balance of \$268,876 this year, an increase of \$68,592. The entire amount is available for spending (*unreserved fund balance*) on behalf of its citizens. The Village's General Fund 2008 year end *fund balance* is \$158,383.

Overview of the Financial Statements

The financial statements are organized so the reader can understand the Village as a financial whole or as an entire operating entity. The statements also provide a detailed look at specific financial conditions.

The Village's basic financial statements are comprised of three components: The government-wide financial statements, fund financial statements, and notes to financial statements. The report also contains other supplementary information in addition to the basic financial statements.

Government-wide Financial Statements

The *statement of net assets* and the *statement of activities* display information about the Village as a whole. These statements include the financial activities of the primary government. For the most part, the effect of interfund activity has been removed from the statements. The statements distinguish between those activities of the Village that are governmental in nature and those that are considered business-type activities. Governmental activities are normally supported by taxes and intergovernmental revenues while business-type activities rely to a significant extent on fees and charges for services.

The statement of net assets presents the financial condition of the governmental and business-type activities of the Village at year end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the Village's governmental activities and business-type activities. Direct expenses are those that are specifically associated with a service, program, or department and, therefore, clearly identifiable to a particular function.

Program revenues include charges paid by the recipient for the goods or services offered by the program, and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the Village with certain limited exceptions. The comparisons of direct expenses with program revenues identifies the extent to which each governmental program or business activity is self-financing or draws from the general revenues of the Village.

With this report, all capital assets and infrastructure are listed for the Village of Sterling. These assets are comprised of buildings and improvements, machinery and equipment, infrastructure and land owned by the Village. These assets total over \$1.5 million.

Fund Financial Statements

The Village uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. There are two categories of funds: *Governmental and Proprietary*.

Governmental Funds:

Governmental funds are those through which most governmental functions of the Village are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purpose for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following are the Village's major governmental funds:

- General Fund – This fund accounts for all financial resources, except those required to be accounted for in another fund. Revenues are derived primarily from property taxes and state revenue.
- Major Street Fund – This fund is used to account for the maintenance and construction of the Village's major street system, including the receipt and expenditure of State motor fuel taxes which are earmarked by law (Act 51 PA 1951, as amended) for major street and highway purposes.
- Local Street Fund – This fund is used to account for the maintenance and construction of the Village's local street system, including the receipt and expenditure of State motor fuel taxes which are earmarked by law (Act 51 PA 1951, as amended) for local street and highway purposes.

Proprietary Funds:

Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position, and cash flows.

The Village's enterprise fund may be used to account for any activity for which a fee is charged to external users (citizens) for goods and services. The following is the Village's major enterprise fund:

- Sewer Fund – This fund is maintained to account for operations of the Village's sewer system. Revenue and expenditure line items reflect maintenance and operation of the sewer system in the Village of Sterling. Revenues required to operate the system are derived primarily from user fees.

Notes to Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided on the Village *government-wide* and *fund* financial statements. The notes to financial statements are presented following the Basic Financial Statements, and provide an expansive and thorough view of various aspects of the audited financial statements.

Other Information:

In addition to the basic financial statements and accompanying notes, this report also presents individual fund statements.

Government -Wide Financial Analysis

Because this is the first year of implementation of Government Accounting Standards Board Statement No. 34, which requires this new reporting model, the following tables present only current year data. In future years, when prior-year information is available, comparative analysis of government-wide data will be presented.

Summary of Net Assets:

The following summarizes the net assets of the Village of Sterling at March 31, 2008:

Net Assets Summary

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
Current Assets	\$ 270,253	\$ 623,658	\$ 893,911
Capital Assets – Net	<u>31,857</u>	<u>609,745</u>	<u>641,602</u>
Total Assets	<u>302,110</u>	<u>1,233,403</u>	<u>1,535,513</u>
 Current Liabilities	 <u>1,377</u>	 <u>0</u>	 <u>1,377</u>
 Net Assets			
Invested in Capital Assets	31,857	609,745	641,602
Unrestricted	<u>268,876</u>	<u>623,658</u>	<u>892,534</u>
 Total Net Assets	 <u><u>\$ 300,733</u></u>	 <u><u>\$ 1,233,403</u></u>	 <u><u>\$ 1,534,136</u></u>

Summary of Changes in Net Assets:

Following is an analysis of the changes in net assets for fiscal year 2008.

Generally speaking, the Village's net assets represent the difference between assets and liabilities. Net assets invested in capital assets consists of capital assets, net of accumulated depreciation. The Village of Sterling, through its governing body, i.e., Village Council, has taken a sensible approach regarding capital asset acquisition. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the Village or through external restrictions imposed by creditors, grantors or laws/regulations of other governments.

It is the Village's practice, in general, to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
Program Revenues:			
Charges for Services	\$ 0	\$ 48,492	\$ 48,492
Operating Grants and Contributions	<u>3,080</u>	<u>0</u>	<u>3,080</u>
Total Program Revenues	<u>3,080</u>	<u>48,492</u>	<u>51,572</u>
General Revenues:			
Property Taxes	64,770	0	64,770
State Revenue Sharing	110,088	0	110,088
Investment Earnings and Miscellaneous	<u>48,672</u>	<u>17,186</u>	<u>65,858</u>
Total General Revenues	<u>223,530</u>	<u>17,186</u>	<u>240,716</u>
Total Revenues	<u>226,610</u>	<u>65,678</u>	<u>292,288</u>
Program Expenses:			
General Government	33,953	0	33,953
Public Works	133,988	0	133,988
Community and Economic Development	2,894	0	2,894
Recreation and Cultural	3,388	0	3,388
Sewer Services	<u>0</u>	<u>66,504</u>	<u>66,504</u>
Total Program Expenses	<u>174,223</u>	<u>66,504</u>	<u>240,727</u>
Change in Net Assets	52,387	(826)	51,561
Beginning Net Assets	<u>248,346</u>	<u>1,234,229</u>	<u>1,482,575</u>
Ending Net Assets	<u>\$ 300,733</u>	<u>\$ 1,233,403</u>	<u>\$ 1,534,136</u>

Governmental Activities

The *Statement of Activities* illustrates, by department, the expense incurred and revenue received.

Total governmental activities reveal revenues of \$3,080 from *Operating Grants and Contributions*. Operating expenses totaled \$174,223 for these same activities. The largest expenses were incurred by Public Works (\$133,988) and General Government (\$33,953).

Business-Type Activities

The Village's main *Business-Type activities* are the Sewer Services. For the most part, Sewer Fund revenues and expenditures reflected maintenance of the status quo as compared to past years. An exception to this observation was an increase in the sewer fee, which increased revenues for *Charges for Services*.

Financial Analysis of Village Funds

As noted earlier in this report, the Village uses fund accounting to ensure and demonstrate compliance with finance-related statutory and legal requirements. A thorough review and examination of fund types will reveal the strengths and weaknesses of its daily operations.

Governmental Funds

Governmental funds are those through which most governmental functions of the Village are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. The difference between governmental fund assets and liabilities is reported as fund balance. The following are the Village's major governmental funds: 1) General fund – accounts for all financial resources, except those required to be accounted for in another fund. Revenues are derived primarily from property taxes and state revenue; 2) Major Street Fund – This fund accounts for the major street operations of the Village. The primary sources of revenue is from State motor fuel taxes which are earmarked by law for major street and highway purposes; and, 3) Local Street fund – This fund accounts for the local street operations of the Village. The primary sources of revenue is from State motor fuel taxes which are earmarked by law for local street and highway purposes.

This year's Village audit, following GASB 34 format, shows 4 funds. The Village Clerk maintains these funds as separate units in the General Ledger.

Enterprise Funds

The Village's enterprise fund provides the same type of information found in the government-wide financial statements. The Sewer services comprise this fund. GASB 34 places such funds under the caption of *Proprietary Funds* under the appropriate statements, i.e., *Statement of Net Assets*, *Statement of Cash Flows*, etc.

Budgetary Highlights

General Fund Budgetary Highlights

The Village's budgets are prepared according to Michigan law. The most significant budgeted fund is the General Fund.

The General Fund actual revenue was \$149,261. That amount is above both the original and final budget estimates of \$110,100. The variance between the actual revenues, the original budget and the final budget was mainly the result of changes in revenues from current property taxes, interest, and rental income.

The actual expenditures of the General Fund were \$99,289, which is below both the original and amended budget estimates of \$120,080. The variance between the actual expenditures, the original budget and the final budget was due to changes in spending in various areas.

The General Fund had total revenues of \$149,261, total expenditures of \$99,289 and an ending fund balance of \$158,383.

Fiscal year 2008 saw the Village's General Fund fund balance increase from \$139,948 to \$158,383. This was caused primarily by a decrease in transfers to other funds.

Capital Asset and Debt Administration

Capital Assets

The Village defines capital assets as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of five years. Such assets are recorded at *historical cost* or *estimated historical cost* if purchased or constructed. Donated capital assets are recorded at estimated FMV (fair market value) at the date of donation.

The Village's infrastructure consists of sewer lines. Improvements are capitalized, i.e., depreciated. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized.

Capital Assets – Governmental Activities beginning and ending balance was \$151,337. Governmental Activities Total Capital Assets – Net of Depreciation was \$31,857.

Capital Assets - Business Type Activities beginning and ending balance was \$1,379,239. Business-Type Activities Total Capital Assets – Net of Depreciation was \$609,745. An expanded and detailed presentation may be seen in Note 5 of the notes to financial statements.

Economic Factors

The Village Council continues to work hard to keep expenditures down and to maintain revenue levels that are within their control. The Village property tax revenues account for approximately 43% of the Village General Fund Revenues.

Revenue sharing from the State of Michigan is the second greatest source of revenue for the Village's General Fund at approximately 31%. As the revenue estimates continue to decline at the state level the Village may lose funds that are currently budgeted. The Village has been able to operate in a streamlined manner, thus building up the General Fund balance to prepare for any reductions that may occur.

The major expenditures for the Village General Fund are for Public Works activities followed by General Government and Other activities.

The Village Council monitors the revenue and expenditures throughout the year and takes appropriate action when the economic factors dictate a change.

Requests for Information

This financial report is designed to provide a general overview of the Village's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Village of Sterling, P.O. Box 165, Sterling, Michigan, 48659.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF NET ASSETS
March 31, 2008

	Primary Government		
	Governmental	Business-Type	
	Activities	Activities	Total
<u>Assets</u>			
Cash and Cash Equivalents (Note 3)	\$ 328,157	\$ 270,114	\$ 598,271
Investments (Note 3)	110,244	142,141	252,385
Receivables:			
Property Taxes	8,587	3,602	12,189
Accounts, Net	0	19,374	19,374
Due from State	11,692	0	11,692
Internal Balances	(188,427)	188,427	0
Noncurrent Assets:			
Capital Assets, Net (Note 5)	31,857	609,745	641,602
Total Assets	<u>302,110</u>	<u>1,233,403</u>	<u>1,535,513</u>
<u>Liabilities</u>			
Accrued Liabilities	<u>1,377</u>	<u>0</u>	<u>1,377</u>
<u>Net Assets</u>			
Invested in Capital Assets	31,857	609,745	641,602
Unrestricted	<u>268,876</u>	<u>623,658</u>	<u>892,534</u>
Total Net Assets	<u>\$ 300,733</u>	<u>\$ 1,233,403</u>	<u>\$ 1,534,136</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF ACTIVITIES
For the Year Ended March 31, 2008

Function/Program					Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Program Revenues			Primary Government		Total
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business- Type Activities	
<u>Primary Government</u>							
Governmental Activities:							
General Government:							
Legislative and Executive	\$ 5,798	\$ 0	\$ 0	\$ 0	\$ (5,798)	\$ 0	\$ (5,798)
Financial and Tax							
Administration	22,227	0	0	0	(22,227)	0	(22,227)
Other General Government	5,928	0	0	0	(5,928)	0	(5,928)
Public Works:							
Other Public Works	133,988	0	3,080	0	(130,908)	0	(130,908)
Community and Economic							
Development	2,894	0	0	0	(2,894)	0	(2,894)
Recreation and Cultural	<u>3,388</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>(3,388)</u>	<u>0</u>	<u>(3,388)</u>
Total Governmental Activities	<u>174,223</u>	<u>0</u>	<u>3,080</u>	<u>0</u>	<u>(171,143)</u>	<u>0</u>	<u>(171,143)</u>
Business-Type Activities:							
Sewer Services	<u>66,504</u>	<u>48,492</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>(18,012)</u>	<u>(18,012)</u>
Total Primary Government	<u>\$ 240,727</u>	<u>\$ 48,492</u>	<u>\$ 3,080</u>	<u>\$ 0</u>	<u>(171,143)</u>	<u>(18,012)</u>	<u>(189,155)</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF ACTIVITIES
For the Year Ended March 31, 2008

					Net (Expense) Revenue and Changes in Net Assets		
					Primary Government		
					Business- Type		
					Activities		
					Total		
Function/Program	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business- Type Activities	Total
General Revenue:							
Property Taxes Levied For:							
General Operating					\$ 64,770	\$ 0	\$ 64,770
State Revenue Sharing					110,088	0	110,088
Interest and Investment							
Earnings					16,858	17,186	34,044
Rent Income					30,793	0	30,793
Other					1,021	0	1,021
Total General Revenue					<u>223,530</u>	<u>17,186</u>	<u>240,716</u>
Change in Net Assets					52,387	(826)	51,561
Net Assets - Beginning					<u>248,346</u>	<u>1,234,229</u>	<u>1,482,575</u>
Net Assets - Ending					<u>\$ 300,733</u>	<u>\$ 1,233,403</u>	<u>\$ 1,534,136</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

BALANCE SHEET
GOVERNMENTAL FUNDS
March 31, 2008

	<u>General Fund</u>	<u>Major Street Fund</u>	<u>Local Street Fund</u>	<u>Total Governmental Funds</u>
<u>ASSETS</u>				
Cash and Cash Equivalents (Note 3)	\$ 133,666	\$ 107,096	\$ 87,395	\$ 328,157
Investments (Note 3)	20,507	59,100	30,637	110,244
Receivables:				
Property Taxes	8,587	0	0	8,587
Due from State	0	9,175	2,517	11,692
Due from Other Funds (Note 4)	<u>14,551</u>	<u>0</u>	<u>16,227</u>	<u>30,778</u>
Total Assets	<u>\$ 177,311</u>	<u>\$ 175,371</u>	<u>\$ 136,776</u>	<u>\$ 489,458</u>
<u>LIABILITIES AND FUND EQUITY</u>				
<u>Liabilities</u>				
Due to Other Funds (Note 4)	\$ 17,551	\$ 17,274	\$ 184,380	\$ 219,205
Accrued Liabilities	<u>1,377</u>	<u>0</u>	<u>0</u>	<u>1,377</u>
Total Liabilities	<u>18,928</u>	<u>17,274</u>	<u>184,380</u>	<u>220,582</u>
<u>Fund Equity</u>				
Fund Balances (Deficit):				
Unreserved:				
Undesignated, Reported In:				
General Fund	158,383	0	0	158,383
Special Revenue Funds	<u>0</u>	<u>158,097</u>	<u>(47,604)</u>	<u>110,493</u>
Total Fund Equity	<u>158,383</u>	<u>158,097</u>	<u>(47,604)</u>	<u>268,876</u>
Total Liabilities and Fund Equity	<u>\$ 177,311</u>	<u>\$ 175,371</u>	<u>\$ 136,776</u>	<u>\$ 489,458</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCES TO
NET ASSETS OF GOVERNMENTAL ACTIVITIES
March 31, 2008

Total Governmental Fund Balances	\$	268,876
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Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds. Capital assets at year end consist of:

Capital Asset Cost	\$	151,337	
Accumulated Depreciation		<u>(119,480)</u>	
			<u>31,857</u>

Total Net Assets - Governmental Activities	\$	<u><u>300,733</u></u>
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The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF REVENUE, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the Year Ended March 31, 2008

	<u>General Fund</u>	<u>Major Street Fund</u>	<u>Local Street Fund</u>	<u>Total Governmental Funds</u>
<u>Revenue</u>				
Property Taxes	\$ 64,770	\$ 0	\$ 0	\$ 64,770
State Grants and Revenue	46,872	52,028	14,268	113,168
Interest and Rentals	36,598	6,393	4,660	47,651
Other Revenue	<u>1,021</u>	<u>0</u>	<u>0</u>	<u>1,021</u>
Total Revenue	<u>149,261</u>	<u>58,421</u>	<u>18,928</u>	<u>226,610</u>
<u>Expenditures</u>				
Current:				
General Government:				
Legislative	4,968	0	0	4,968
Chief Executive	600	0	0	600
Financial and Tax Administration	21,297	0	0	21,297
Other General Government	3,858	0	0	3,858
Public Works	42,789	40,251	18,478	101,518
Community and Economic Development	2,695	0	0	2,695
Recreation and Cultural	3,388	0	0	3,388
Other	<u>19,694</u>	<u>0</u>	<u>0</u>	<u>19,694</u>
Total Expenditures	<u>99,289</u>	<u>40,251</u>	<u>18,478</u>	<u>158,018</u>
Excess of Revenue Over Expenditures	<u>49,972</u>	<u>18,170</u>	<u>450</u>	<u>68,592</u>
<u>Other Financing Sources (Uses)</u>				
Operating Transfers In	0	0	31,537	31,537
Operating Transfers Out	<u>(31,537)</u>	<u>0</u>	<u>0</u>	<u>(31,537)</u>
Total Other Financing Sources (Uses)	<u>(31,537)</u>	<u>0</u>	<u>31,537</u>	<u>0</u>
Excess of Revenue and Other Sources Over Expenditures and Other Uses	18,435	18,170	31,987	68,592
Fund Balances (Deficit) - Beginning of Year	<u>139,948</u>	<u>139,927</u>	<u>(79,591)</u>	<u>200,284</u>
Fund Balances (Deficit) - End of Year	<u>\$ 158,383</u>	<u>\$ 158,097</u>	<u>\$ (47,604)</u>	<u>\$ 268,876</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

RECONCILIATION OF THE STATEMENT OF REVENUE, EXPENDITURES
AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the Year Ended March 31, 2008

Total Net Change in Fund Balances - Governmental Funds	\$ 68,592
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.	
Current Year Depreciation Expense	<u>(16,205)</u>
Change in Net Assets of Governmental Activities	\$ <u>52,387</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF NET ASSETS
PROPRIETARY FUND
March 31, 2008

	<u>Enterprise Fund</u>
	<u>Sewer Fund</u>
<u>Assets</u>	
Current Assets:	
Cash and Cash Equivalents (Note 3)	\$ 270,114
Investments (Note 3)	142,141
Receivables:	
Property Taxes	3,602
Accounts, Net	19,374
Due from Other Funds (Note 4)	<u>188,427</u>
Total Current Assets	623,658
Noncurrent Assets:	
Capital Assets, Net (Note 5)	<u>609,745</u>
Total Assets	<u>1,233,403</u>
<u>Liabilities</u>	
Current Liabilities:	
Accounts Payable	<u>0</u>
<u>Net Assets</u>	
Invested In Capital Assets	609,745
Unrestricted	<u>623,658</u>
Total Net Assets	\$ <u>1,233,403</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS
 PROPRIETARY FUND
For the Year Ended March 31, 2008

	<u>Enterprise Fund</u>
	<u>Sewer Fund</u>
<u>Operating Revenue</u>	
Charges For Services	\$ <u>48,492</u>
<u>Operating Expenses</u>	
Salaries and Wages	6,331
Depreciation	28,175
Equipment Rental	5,143
Office Supplies	293
Postage	287
Repair and Maintenance	14,734
Utilities	5,259
Other	<u>6,282</u>
Total Operating Expenses	<u>66,504</u>
Operating Loss	(18,012)
<u>Nonoperating Revenue (Expenses)</u>	
Interest and Investment Earnings	<u>17,186</u>
Change in Net Assets	(826)
Net Assets - Beginning of Year	<u>1,234,229</u>
Net Assets - End of Year	<u>\$ 1,233,403</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF CASH FLOWS
PROPRIETARY FUND
For the Year Ended March 31, 2008

	<u>Enterprise Fund</u>
	<u>Sewer Fund</u>
<u>Cash Flows From Operating Activities</u>	
Receipts From Customers	\$ 44,069
Payments for Supplies and Services	(31,998)
Payments to Employees for Services	<u>(6,331)</u>
Net Cash Provided by Operating Activities	<u>5,740</u>
<u>Cash Flows From Non-Capital Financing Activities</u>	
Special Assessments Received	61
Interest Received on Assessments	4
Cash Received from Other funds	<u>16,342</u>
Net Cash Provided by Non-Capital Financing Activities	<u>16,407</u>
<u>Cash Flows From Investing Activities</u>	
Redemption of Investment Securities	97,611
Interest on Investments	<u>12,174</u>
Net Cash Provided by Investing Activities	<u>109,785</u>
Net Increase in Cash and Cash Equivalents	131,932
Cash and Cash Equivalents at Beginning of Year (Note 1)	<u>138,182</u>
Cash and Cash Equivalents at End of Year (Note 1)	<u>\$ 270,114</u>
<u>Reconciliation of Operating Loss to Net Cash Provided by Operating Activities</u>	
Operating Loss	\$ (18,012)
Adjustments to Reconcile Operating Loss to Net Cash Provided by Operating Activities:	
Depreciation Expense	28,175
Change in Assets and Liabilities:	
Accounts and Taxes Receivable	<u>(4,423)</u>
Net Cash Provided by Operating Activities	<u>\$ 5,740</u>

The accompanying notes to financial statements are an integral part of this statement.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Village of Sterling (Village) conform to accounting principles generally accepted in the United States of America (GAAP) applicable to governments. Private-sector standards of accounting issued after November 30, 1989, are generally followed in both the government-wide and enterprise fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board. The following is a summary of the significant accounting policies:

A. Description of Village Operations and Fund Types

The Village of Sterling operates under an elected Council of nine members and provides services to its residents in many areas including maintenance of major and local streets, and street lighting. All activities over which the Village exercises oversight responsibility have been included in the reporting entity. Oversight responsibility is determined by factors such as financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters of the entity.

B. Reporting Entity

A reporting entity is composed of the primary government, component units, and other organizations that are included to ensure the financial statements of the Village are not misleading. The primary government of the Village consists of all funds, departments, boards, and agencies that are not legally separate from the Village.

Component units are legally separate organizations for which the Village is financially accountable. The Village is financially accountable for an organization if the Village appoints a voting majority of the organization's governing board and (1) the Village is able to significantly influence the programs of services performed or provided by the organization; or (2) the Village is legally entitled to or can otherwise access the organization's resources; the Village is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or the Village is obligated for the debt of the organization. Component units may also include organizations for which the Village approves the budget, the issuance of debt, or the levying of taxes. The Village does not have any component units.

C. Basis of Presentation

The Village's basic financial statements consist of government-wide financial statements, including a statement of net assets and a statement of activities, and fund financial statements which provide a more detailed level of financial information.

Government-Wide Financial Statements

The statement of net assets and the statement of activities display information about the Village as a whole. These statements include the financial activities of the primary government. For the most part, the effect of interfund activity has been removed from the statements. The statements distinguish between those activities of the Village that are governmental and those that are considered business-type activities. Governmental activities are normally supported by taxes and intergovernmental revenues while business-type activities rely to a significant extent on fees and charges for support.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Basis of Presentation (Continued)

The statement of net assets presents the financial condition of the governmental and business-type activities of the Village at year end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the Village's governmental and business-type activities. Direct expenses are those that are specifically associated with a service, program, or department and, therefore, clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the Village, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental program or business activity is self-financing or draws from the general revenues of the Village.

Fund Financial Statements

During the year, the Village segregates transactions related to certain Village functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the Village at this more detailed level. The focus of governmental and proprietary fund financial statements is on major funds. Each major fund is presented in a separate column.

D. Fund Accounting

The Village uses funds to maintain its financial records during the fiscal year. Fund accounting is designed to demonstrate legal compliance and to aid management by segregating transactions related to certain Village functions or activities. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. There are two categories of funds: governmental and proprietary.

Governmental Funds

Governmental funds are those through which most governmental functions of the Village are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following are the Village's major governmental funds:

General Fund - This fund accounts for all financial resources, except those required to be accounted for in another fund. Revenues are derived primarily from property taxes and state revenue.

Major Street Fund - This fund is used to account for the maintenance and construction of the Village's major street system, including the receipt and expenditure of State motor fuel taxes which are earmarked by law (Act 51 PA 1951, as amended) for major street and highway purposes.

Local Street Fund - This fund is used to account for the maintenance and construction of the Village's local street system, including the receipt and expenditure of State motor fuel taxes which are earmarked by law (Act 51 PA 1951, as amended) for local street and highway purposes.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Fund Accounting (Continued)

Proprietary Funds

Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position, and cash flows.

The Village's enterprise fund may be used to account for any activity for which a fee is charged to external users for goods or services. The following is the Village's major enterprise fund:

Sewer Fund - This fund accounts for fees collected for sewer services provided by the Village.

E. Measurement Focus

Government-Wide Financial Statements

The government-wide financial statements are prepared using a flow of economic resources measurement focus.

All assets and all liabilities associated with the operation of the Village are included on the statement of net assets.

Fund Financial Statements

All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are generally included on the balance sheet. The statement of revenue, expenditures, and changes in fund balances reflects the sources (i.e., revenues and other financial sources) and uses (i.e., expenditures and other financial uses) of current financial resources. This approach differs from the manner in which the governmental activities of the government-wide financial statements are prepared. Governmental fund financial statements, therefore, include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the fund financial statements for governmental funds.

Like the government-wide financial statements, the enterprise funds are accounted for using a flow of economic resources measurement focus. All assets and all liabilities associated with the operation of these funds are included on the statement of net assets. The statement of changes in revenue, expenses, and changes in net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in total net assets. The statement of cash flows reflects how the Village finances and meets the cash flow needs of its enterprise activities.

F. Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide and proprietary funds financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Differences in the accrual and modified accrual basis of accounting arise in the recognition of revenue, the recording of deferred revenue, and in the presentation of expenses versus expenditures.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

F. Basis of Accounting (Continued)

Revenues – Exchange and Non-exchange Transactions

Revenues resulting from exchange transactions, in which each party receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recorded in the fiscal year in which the resources are measurable and available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the Village, available means expected to be received within 60 days of the fiscal year-end.

Nonexchange transactions, in which the Village receives value without directly giving equal value in return, include property taxes, sales taxes, grants, entitlements and donations. On the accrual basis, revenue from property taxes is recognized in the year for which the taxes are levied. Revenue from sales taxes is recognized in the period in which the sales are made. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the Village must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the Village on a reimbursement basis. On a modified accrual basis, revenues from nonexchange transactions must also be available before they can be recognized.

Under the modified accrual basis, the following revenue sources are considered to be both measurable and available at year-end: charges for services, fines and forfeitures, state-levied locally shared taxes (including sales tax), grants, interest, rent and various other items.

Expenses/Expenditures

On the accrual basis of accounting, expenses are recognized at the time they are incurred.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation and amortization, are not recognized in governmental funds.

G. Cash and Cash Equivalents

For presentation on the financial statements, investments in the cash management pools and investments with an original maturity of three months or less at the time they are purchased by the Village are considered to be cash equivalents. Investments with an initial maturity of more than three months are reported as investments.

Investments are reported at fair value, except for repurchase agreements and certificates of deposit which are reported at cost which approximates fair value. Fair value is based on quoted market prices. Mutual funds are reported at current share price.

H. Receivables

Receivables generally consist of accounts (fees) and property taxes. All receivables are net of estimated uncollectible accounts. Receivables are recognized to the extent the amounts are determined material and substantiated, not only by supporting documentation but also by a reasonable systematic method of determining their existence, completeness, valuation, and collectibility.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

H. Receivables (Continued)

The allowance for doubtful accounts at March 31, 2008 was \$0.

I. Interfund Receivables and Payables

On fund financial statements, receivables and payables resulting from short-term interfund loans or interfund services provided and used are classified as "due from/to other funds". Interfund balances within governmental activities and within business-type activities are eliminated on the government-wide statement of net assets. The only interfund balances which remain on the government-wide statement of net assets are those between governmental and business-type activities. These amounts are reflected as "Internal Balances".

J. Capital Assets

General capital assets are capital assets which are associated with and generally arise from governmental activities. They generally result from expenditures in governmental funds. General capital assets are reported in the governmental activities column of the government-wide statement of net assets, but are not reported in the fund financial statements. Capital assets used by the enterprise funds are reported in both the business-type activities column of the government-wide statement of net assets and in the respective funds.

Capital assets are defined by the government as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Improvements are capitalized and depreciated over the remaining useful lives of the related capital assets. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized.

Capital assets are depreciated using the straight-line method over the following useful lives:

<u>Descriptions</u>	<u>Estimated Lives</u>
Buildings and Improvements	25 - 50 years
Land Improvements	10 - 20 years
Machinery and Equipment	5 - 10 years
Utility Systems	25-40 years

K. Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities and long-term obligations are reported in the government-wide financial statements. All payables, accrued liabilities, and long-term obligations payable from the enterprise fund are reported on the enterprise fund statement. In general, payables and accrued liabilities that will be paid from governmental funds are reported as a liability in the fund financial statements at the time they are incurred, to the extent that they will be paid from current, expendable, financial resources. However, bonds and other long-term obligations, compensated absences, claims and judgments, contractually required pension contributions and special termination benefits that are paid from governmental funds are recognized as liabilities in the fund financial statements only to the extent that they are due for payment during the current year.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

L. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets consists of capital assets net of accumulated depreciation. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the Village or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. The Village's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

M. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the enterprise fund. For the Village, these revenues are charges for services for sewer usage. Operating expenses are the necessary costs incurred to provide the service that is the primary activity of the fund. Revenues and expenses not meeting these definitions are reported as nonoperating.

N. Interfund Activity

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/ expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds. Repayments from funds responsible for particular expenditures/ expenses to the funds that initially paid for them are not presented on the financial statements.

O. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of the Council and that are either unusual in nature or infrequent in occurrence. Neither type of transaction occurred during the fiscal year ended March 31, 2008.

P. Budgets and Budgetary Accounting

The Village of Sterling normally follows these procedures in establishing the budgetary data reflected in the financial statements.

1. Prior to March 1, the Village President submits to the Village Council a proposed operating budget for the fiscal year commencing the following April 1. This operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted at the governmental center to obtain taxpayer comments.
3. Prior to April 1, the budget is legally enacted through passage of an ordinance.
4. All budget appropriations lapse at year-end. Budgetary amounts reported herein are as originally adopted, and as amended by the Village Council throughout the operating year.

The Village adopts budgets for the General Fund and Special Revenue Funds.

The budgets of the Village are prepared on the same basis of accounting as the financial statement presentation. The budgets were adopted at the activity level.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. Budgets and Budgetary Accounting (Continued)

Budgets shown in the financial statements are adopted on a basis consistent with generally accepted accounting principles, and consist only of those amounts contained in the formal budget approved and amended by the Village Council.

Q. Use of Estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

NOTE 2 - CHANGE IN ACCOUNTING PRINCIPLES

Change in Accounting Principles

For 2008, the Village has implemented Governmental Accounting Standards Board (GASB) Statement Number 34, "Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments"; GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus"; and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" in their entirety as required by the Local Audit and Finance Division of the Treasury Department of the State of Michigan.

GASB Statement No. 34 creates new basic financial statements for reporting on the Village's financial activities. The financial statements include government-wide financial statements prepared on the accrual basis of accounting. The government-wide financial statements split the Village's programs between governmental activities and business type activities.

GASB Statement No. 37 makes certain clarifications regarding escheat property and modifies several provisions of GASB Statement No. 34, including the Management's Discussion and Analysis. GASB Statement No. 38 modifies, establishes, and rescinds certain financial statement disclosure requirements.

NOTE 3 - DEPOSITS AND INVESTMENTS

At year-end, the Village's deposits and investments were reported in the basic financial statements in the following categories:

	<u>Governmental Activities</u>	<u>Business- Type Activities</u>	<u>Total Primary Government</u>
Cash and Cash Equivalents	\$ 328,157	\$ 270,114	\$ 598,271
Investments	<u>110,244</u>	<u>142,141</u>	<u>252,385</u>
Total	<u>\$ 438,401</u>	<u>\$ 412,255</u>	<u>\$ 850,656</u>

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 3 - DEPOSITS AND INVESTMENTS (CONTINUED)

The breakdown between deposits and investments is as follows:

	<u>Primary Government</u>
Bank Deposits (Checking Accounts and Certificates of Deposit)	\$ 350,832
Investments in Financial Institution Pooled Funds	<u>499,824</u>
Total	<u>\$ 850,656</u>

As of March 31, 2008, the Village had the following investments.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Specific Identification Maturities</u>
Primary Government: Investment Pools	\$ <u>499,824</u>	Daily

Interest Rate Risk

In accordance with its investment policy, the Village will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by; structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market; and investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds, or similar investment pools and limiting the average maturity in accordance with the Village's known cash requirements.

Credit Risk

State law authorizes investments in investment pools as authorized by the Surplus Funds Investment Pool Act, Act No. 367 of the Public Acts of 1982, being sections 129.111 to 129.118 of the Michigan Compiled Laws, composed entirely of instruments that are legal for direct investment by a local government unit in Michigan. The Village's investment pools are unrated.

Custodial Credit Risk - Deposits

In the case of deposits, this is the risk that in the event of a bank failure, the Village's deposits may not be returned to it. As of March 31, 2008, \$89,591 of the Village's bank balance of \$351,593 was exposed to custodial credit risk because it was uninsured and uncollateralized.

Concentration of Credit Risk

The Village will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the Village's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 3 - DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk – Investments

For an investment, this is the risk that, in the event of the failure of the counterparty, the Village will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

The Village will minimize custodial credit risk, by; limiting investments to the types of securities approved in the Village's investment policy which is in accordance with State law.

Foreign Currency Risk

The Village's investment policy does not address foreign currency risk.

Investments

The Village Council has adopted an investment policy in accordance with Act 196, PA 1997 which authorizes the Village to deposit and invest in the following:

- λ Accounts of federally insured banks, credit unions and savings and loan associations
- λ Bonds and other direct obligations of the United States or an agency or instrumentality of the United States
- λ United States government or federal agency obligation repurchase agreements
- λ Banker's acceptances of United States banks
- λ Commercial paper rated within the two highest classifications by not less than two standard rating services which mature not more than 270 days after the date of purchase
- λ Mutual funds registered under the Investment Company Act of 1940, Title I of Chapter 686, 54 Stat. 789 15 U.S.C. 80a-1 to 80a-3 and 80a-4 to 80a-64 with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation

Michigan law requires that public funds may not be deposited in financial institutions that do not maintain an office in Michigan. The Village's deposits and investments are in accordance with statutory authority.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 4 - INTERFUND RECEIVABLES AND PAYABLES

The amounts of interfund receivables and payables as of March 31, 2008 were as follows:

<u>Fund</u>	<u>Interfund Receivable</u>	<u>Interfund Payable</u>
Major Governmental Funds:		
General Fund	\$ 14,551	\$ 17,551
Major Street Fund	0	17,274
Local Street Fund	<u>16,227</u>	<u>184,380</u>
Total Major Governmental Funds	30,778	219,205
Major Enterprise Funds:		
Sewer Fund	<u>188,427</u>	<u>0</u>
	<u>\$ 219,205</u>	<u>\$ 219,205</u>

The amounts of interfund receivables and payables for individual funds as of March 31, 2008 were as follows:

<u>Fund</u>	<u>Interfund Receivable</u>	<u>Fund</u>	<u>Interfund Payable</u>
General Fund	\$ 14,551	Major Street Fund	\$ 14,551
Local Street Fund	16,227	General Fund	16,227
Sewer Fund	1,324	General Fund	1,324
Sewer Fund	2,723	Major Street Fund	2,723
Sewer Fund	<u>184,380</u>	Local Street Fund	<u>184,380</u>
Total	<u>\$ 219,205</u>	Total	<u>\$ 219,205</u>

These balances result from the time lag between the dates that interfund goods and services are provided, transactions are recorded in the accounting system, and payments between funds are made.

The amount of the interfund receivable/payable between the Sewer Fund and the Local Street Fund not expected to be repaid within one year of March 31, 2008 was \$168,760.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 5 - CAPITAL ASSETS

Capital asset activity of the primary government for the fiscal year ended March 31, 2008, was as follows:

	Balance 04/01/07	Additions	Deletions	Balance 03/31/08
<u>Governmental Activities</u>				
Capital Assets Not Being Depreciated:				
Land	\$ 22,438	\$ 0	\$ 0	\$ 22,438
Capital Assets Being Depreciated:				
Buildings and Improvements	22,343	0	0	22,343
Machinery and Equipment	106,556	0	0	106,556
Subtotal	128,899	0	0	128,899
Less Accumulated Depreciation for:				
Buildings and Improvements	(22,343)	0	0	(22,343)
Machinery and Equipment	(80,932)	(16,205)	0	(97,137)
Subtotal	(103,275)	(16,205)	0	(119,480)
Capital Assets Being Depreciated	25,624	(16,205)	0	9,419
Governmental Activities Total				
Capital Assets - Net of Depreciation	\$ 48,062	\$ (16,205)	\$ 0	\$ 31,857
	Balance 04/01/07	Additions	Deletions	Balance 03/31/08
<u>Business-Type Activities</u>				
Capital Assets Not Being Depreciated:				
Land	\$ 5,408	\$ 0	\$ 0	\$ 5,408
Capital Assets Being Depreciated:				
Machinery and Equipment	21,911	0	0	21,911
Sewer System	1,351,920	0	0	1,351,920
Subtotal	1,373,831	0	0	1,373,831
Less Accumulated Depreciation for:				
Machinery and Equipment	(15,765)	(797)	0	(16,562)
Sewer System	(725,554)	(27,378)	0	(752,932)
Subtotal	(741,319)	(28,175)	0	(769,494)
Business-Type Activities Total				
Capital Assets - Net of Depreciation	\$ 637,920	\$ (28,175)	\$ 0	\$ 609,745

Depreciation expense was charged to programs of the primary government as follows:

<u>Governmental Activities</u>	
General Government:	
Public Works	\$ 16,205
<u>Business-Type Activities</u>	
Sewer	\$ 28,175

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 6 - PROPERTY TAXES

Property taxes include amounts levied against all real property and tangible personal property located in the Village. Properties are assessed as of December 31 and the related property taxes become a lien on December 1 of the following year. These taxes are due on February 14 with the final collection date of February 28 before they are added to the County tax rolls. For the current year, the taxable value for properties located within the Village was \$8,045,866. The 2007 operating tax rates are currently 8 mills for operations.

NOTE 7 - OPERATING TRANSFERS

During the year ended March 31, 2008, the following transfers were made:

<u>Description</u>	<u>Operating Transfers In</u>	<u>Operating Transfers Out</u>
<u>Major Funds</u>		
Major Governmental Funds:		
General Fund	\$ 0	\$ 31,537
Local Street Fund	<u>31,537</u>	<u>0</u>
Total Major Funds	<u>\$ 31,537</u>	<u>\$ 31,537</u>

During the year ended March 31, 2008, the following individual fund transfers were made:

<u>Fund</u>	<u>Transfer In</u>	<u>Fund</u>	<u>Transfer Out</u>
Local Street Fund	\$ <u>31,537</u>	General Fund	\$ <u>31,537</u>

Transfers are used to move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, and use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

NOTE 8 - FUND BALANCE (DEFICIT)

A deficit unreserved fund balance of \$47,604 existed at March 31, 2008 in the Local Street Fund. The Village filed a deficit elimination plan with the Michigan Department of Treasury after the March 31, 2007 fiscal year end that eliminates the deficit within five years.

NOTE 9 - EXCESS OF EXPENDITURES OVER APPROPRIATION IN BUDGETARY FUNDS

P.A. 621 of 1978, Section 18(1), as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated.

In the body of the financial statements, the Village's actual expenditures and budgeted expenditures for the budgetary funds have been shown on an activity basis. The approved budgets of the Village for these budgetary funds were adopted at the activity level.

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 9 - EXCESS OF EXPENDITURES OVER APPROPRIATION IN BUDGETARY FUNDS (CONTINUED)

During the year ended March 31, 2008, the Village incurred expenditures which were in excess of the amounts appropriated as follows:

<u>Fund/Activity</u>	<u>Total</u> <u>Appropriations</u>	<u>Amount of</u> <u>Expenditures</u>	<u>Budget</u> <u>Variance</u>
General Fund/Financial and Tax Administration	\$ 20,790	\$ 21,297	\$ 507
General Fund/Community and Economic Development	\$ 2,000	\$ 2,695	\$ 695
General Fund/Recreation and Cultural	\$ 2,400	\$ 3,388	\$ 988
General Fund/Operating Transfers Out	\$ 14,000	\$ 31,537	\$ 17,537

NOTE 10 - RETIREMENT SYSTEM - MERS OPERATED

Plan Description

The Village's defined benefit pension plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The plan is affiliated with the Municipal Employees Retirement System (MERS) of Michigan, an agent multiple-employer, state-wide, public employee pension created under Public Act 135 of 1945, and now operating under Public Act 220 of 1996, and the MERS Plan Document as revised. Any municipality within the State may elect to become a participating member of MERS or elect to terminate participation by a majority vote of the municipality's governing body. Changes in benefit coverage are available to bargaining units after approval by a majority of the municipality's governing body. The MERS of Michigan issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to MERS of Michigan, 1134 Municipal Way, Lansing, Michigan 48917 or by calling 1-800-767-6377.

Funding Policy

The Village is required to contribute at an actuarially determined rate. The current rate is 0% of annual covered payroll for General Members. There is no current contribution requirement for plan members. If a member leaves the employ of the Village, or dies, without a retirement allowance or other benefit payable on his/her account, the members' accumulated contributions (with interest) are refunded with spousal consent to the member, if living, or to the members' surviving spouse or beneficiary. The contribution requirements are established and may be amended by the MERS Retirement Board.

Annual Pension Cost

For the year ended March 31, 2008, the Village's annual pension cost of \$1,795 was equal to the Village's actual contributions and above the required contribution amount of \$0. The required contribution was determined as part of the December 31, 2007 actuarial valuation using the entry age normal cost method. The actuarial assumptions included (a) 8% investment rate of return, (b) projected salary increases of 4.5% per year compounded annually, and (c) additional projected salary increases of 0% to 8.4% per year, depending on age, attributable to merit, longevity and promotions. Both (a) and (b) include an inflation component. The Village's net pension obligation has been fully funded at March 31, 2008.

The Village adopted GASB 27 Accounting for Pensions by State and Local Governmental Employer. The following pension information is presented in accordance with GASB 27:

VILLAGE OF STERLING
Arenac County, Michigan

NOTES TO FINANCIAL STATEMENTS
For the Year Ended March 31, 2008

NOTE 10 - RETIREMENT SYSTEM - MERS OPERATED (CONTINUED)

Actuarial Accrued Liability at December 31, 2007

Actuarial Valuation

Retirees and beneficiaries currently receiving benefits	\$ 47,988
Terminated employees (vested former members) not yet receiving benefits	0
Non-vested terminated employees (Pending refunds of accumulated member contributions)	0
Current employees -	
Accumulated employee contributions including allocated investment income	27,171
Employer financed	<u>25,917</u>
Total Actuarial Accrued Liability	101,076
Net assets available for benefits at actuarial value (Market value was \$231,348)	<u>228,680</u>
Unfunded (Overfunded) Actuarial Accrued Liability	<u>\$ (127,604)</u>

Trend Information

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
March 31, 2006	\$ 0	100 %	\$ 0
March 31, 2007	\$ 0	100 %	\$ 0
March 31, 2008	\$ 1,795	100 %	\$ 0

Schedule of Funding Progress

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Liability (AAL) - Entry Age (b)</u>	<u>Unfunded AAL (UAAL) (b-a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percentage of Covered Payroll ((b-a) / c)</u>
12/31/05	\$ 199,376	\$ 84,783	\$ (114,593)	235 %	\$ 35,432	(323)%
12/31/06	\$ 214,157	\$ 85,096	\$ (129,061)	252 %	\$ 31,127	(415)%
12/31/07	\$ 228,680	\$ 101,076	\$ (127,604)	226 %	\$ 32,086	(398)%

NOTE 11 - UNEMPLOYMENT COMPENSATION

The Village is subject to the Michigan Employment Security Act and has elected the reimbursement method of financing. Under this method, the Village must reimburse the Employment Agency for all benefits charged against the Village. Accrued unemployment compensation was \$0 as of March 31, 2008.

NOTE 12 - RISK MANAGEMENT

The Village is exposed to various risks of loss related to property loss, torts, errors and omissions, employee injuries and natural disasters. The Village has purchased commercial insurance for risks of loss. Settled claims for the commercial insurance have not exceeded the amount of insurance coverage in any of the past three years.

REQUIRED SUPPLEMENTARY INFORMATION

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF REVENUE, EXPENDITURES AND
CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND
For the Year Ended March 31, 2008

	Original Budget	Final Amended Budget	Actual	Variance - Favorable (Unfavorable)
<u>Revenue</u>				
Property Taxes	\$ 44,000	\$ 44,000	\$ 64,770	\$ 20,770
State Grants and Revenue	45,000	45,000	46,872	1,872
Interest and Rentals	21,000	21,000	36,598	15,598
Other Revenue	100	100	1,021	921
Total Revenue	<u>110,100</u>	<u>110,100</u>	<u>149,261</u>	<u>39,161</u>
<u>Expenditures</u>				
Current:				
General Government:				
Legislative	6,310	6,310	4,968	1,342
Chief Executive	1,000	1,000	600	400
Financial and Tax Administration	20,790	20,790	21,297	(507)
Other General Government	9,580	9,580	3,858	5,722
Public Works	48,000	48,000	42,789	5,211
Community and Economic Development	2,000	2,000	2,695	(695)
Recreation and Cultural	2,400	2,400	3,388	(988)
Other	25,000	25,000	19,694	5,306
Capital Outlay	<u>5,000</u>	<u>5,000</u>	<u>0</u>	<u>5,000</u>
Total Expenditures	<u>120,080</u>	<u>120,080</u>	<u>99,289</u>	<u>20,791</u>
Excess of Revenue Over (Under) Expenditures	(9,980)	(9,980)	49,972	59,952
<u>Other Financing Uses</u>				
Operating Transfers Out	<u>(14,000)</u>	<u>(14,000)</u>	<u>(31,537)</u>	<u>(17,537)</u>
Excess of Revenue Over (Under) Expenditures and Other Uses	(23,980)	(23,980)	18,435	42,415
Fund Balances - Beginning of Year	<u>139,948</u>	<u>139,948</u>	<u>139,948</u>	<u>0</u>
Fund Balances - End of Year	<u>\$ 115,968</u>	<u>\$ 115,968</u>	<u>\$ 158,383</u>	<u>\$ 42,415</u>

VILLAGE OF STERLING
Arenac County, Michigan

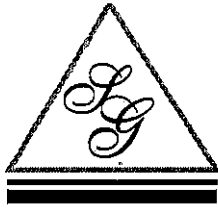
STATEMENT OF REVENUE, EXPENDITURES AND
 CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
 MAJOR STREET FUND - SPECIAL REVENUE FUND
For the Year Ended March 31, 2008

	<u>Original Budget</u>	<u>Final Amended Budget</u>	<u>Actual</u>	<u>Variance - Favorable (Unfavorable)</u>
<u>Revenue</u>				
State Grants and Revenue	\$ 55,000	\$ 55,000	\$ 52,028	\$ (2,972)
Interest and Rentals	<u>3,500</u>	<u>3,500</u>	<u>6,393</u>	<u>2,893</u>
Total Revenue	58,500	58,500	58,421	(79)
<u>Expenditures</u>				
Current:				
Public Works	<u>47,450</u>	<u>47,450</u>	<u>40,251</u>	<u>7,199</u>
Excess of Revenue Over Expenditures	11,050	11,050	18,170	7,120
Fund Balances - Beginning of Year	<u>139,927</u>	<u>139,927</u>	<u>139,927</u>	<u>0</u>
Fund Balances - End of Year	<u>\$ 150,977</u>	<u>\$ 150,977</u>	<u>\$ 158,097</u>	<u>\$ 7,120</u>

VILLAGE OF STERLING
Arenac County, Michigan

STATEMENT OF REVENUE, EXPENDITURES AND
CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
LOCAL STREET FUND - SPECIAL REVENUE FUND
For the Year Ended March 31, 2008

	Original Budget	Final Amended Budget	Actual	Variance - Favorable (Unfavorable)
<u>Revenue</u>				
State Grants and Revenue	\$ 14,000	\$ 14,000	\$ 14,268	\$ 268
Interest and Rentals	<u>5,000</u>	<u>5,000</u>	<u>4,660</u>	<u>(340)</u>
Total Revenue	19,000	19,000	18,928	(72)
<u>Expenditures</u>				
Current:				
Public Works	<u>48,120</u>	<u>48,120</u>	<u>18,478</u>	<u>29,642</u>
Excess of Revenue Over (Under) Expenditures	(29,120)	(29,120)	450	29,570
<u>Other Financing Sources</u>				
Operating Transfers In	<u>14,000</u>	<u>14,000</u>	<u>31,537</u>	<u>17,537</u>
Excess of Revenue and Other Sources Over (Under) Expenditures	(15,120)	(15,120)	31,987	47,107
Fund Balances (Deficit) - Beginning of Year	<u>(79,591)</u>	<u>(79,591)</u>	<u>(79,591)</u>	<u>0</u>
Fund Balances (Deficit) - End of Year	<u>\$ (94,711)</u>	<u>\$ (94,711)</u>	<u>\$ (47,604)</u>	<u>\$ 47,107</u>



Stephenson, Gracik & Co., P.C.

Certified Public Accountants & Consultants

Alan J. Stephenson, CPA
Gerald D. Gracik Jr., CPA
James J. Gracik, CPA
Donald W. Brannan, CPA
Kyle E. Troyer, CPA

Herman A. Bertuleit, CPA

August 27, 2008

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Members of the Village Council
Village of Sterling
Arenac County, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, and each major fund of the Village of Sterling, Arenac County, Michigan, as of and for the year ended March 31, 2008, which collectively comprise the Village of Sterling's basic financial statements and have issued our report thereon dated August 27, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Village of Sterling's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Village of Sterling's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Village of Sterling's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Village of Sterling's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Village of Sterling's financial statements that is more than inconsequential will not be prevented or detected by the Village of Sterling's internal control. We consider the deficiencies described below to be significant deficiencies in internal control over financial reporting.

Financial Statement Preparation

The Village of Sterling prepares various financial information throughout the year to assess operations and the financial condition of the Village. However, prior to the closing of the year end, various entries material to the financial statements were proposed by our firm. Also, the Village relies on our firm to assist in preparing the annual financial report in accordance with Generally Accepted Accounting Principles.

Members of the Village Council
Village of Sterling
August 27, 2008

The Village of Sterling has individuals on staff to review that the financial report is accurate and the financial information reflects the recording of the proposed entries, however, not to review and determine that the financial report is a complete presentation in accordance with Generally Accepted Accounting Principles. As a result, the Village is considered to have a significant control deficiency, since reporting errors or omissions could occur in the preparation of the annual financial report that would be departures from Generally Accepted Accounting Principles and the Village would not be in a position to detect the errors or omissions.

Separation of Duties in the Performance of Functions

The present system of internal accounting controls does not provide for separation of duties in the performance of functions. In our opinion, the system is adequate to account for the financial activity of the Village of Sterling but could be strengthened by a few minor changes in the personnel assigned to perform certain functions.

We recommend that the cash receipts and cash disbursements functions be handled by different individuals. Cash receiving should be centralized in a person without authority to sign checks and without access to noncash accounting records and not involved in reconciling bank accounts. A different person should prepare checks and reconcile the bank accounts.

General Ledger Activity

During our fieldwork, we again noted various improper postings of receipts and disbursements and inconsistent treatment of revenue and expense transactions. We also noted that the Village did not record all of the receivables in the general ledger. We recommend that the Village post receipts and disbursements to the proper accounts in accordance with the State chart of accounts. We also recommend that the Village record all receivables in the general ledger system at the time that the billings are generated.

Bank Accounts

During our fieldwork, we again noted that although bank reconciliations were performed on the cash accounts, there were outstanding items on the reconciliations that had cleared the bank and that should be removed and there was disbursement activity that was double booked to the general ledger. This activity caused the general ledger to not be in agreement with the actual bank activity. Based on the above situation it appears that the cash controls and reconciliation process is not operating effectively. We recommend that the Village take better care to reconcile the cash balances per the computer system on a monthly basis.

Unrecorded Assets

During our fieldwork it was brought to our attention that the Village opened a new bank account in the current year that was not recorded in the general ledger. This activity was recorded through audit adjustments. After the audit was complete, the Village obtained the necessary guidance to record the account properly in the general ledger. We recommend that the Village record all assets in the general ledger system as of the date they are obtained.

Village Board Reports

The Village Council was not provided with quarterly financial and budget reports as required by the State of Michigan Accounting Manual. As a result the Village did not monitor its budget during the year. We recommend that the Village Clerk provide at least quarterly reports to the Village Council, for each fund, that include a balance sheet and profit and loss statements with a budget to actual presentation. These reports will be useful in controlling the budget as well as making other necessary financial decisions.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Village of Sterling's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first

Members of the Village Council
Village of Sterling
August 27, 2008

paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiencies described above to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Village of Sterling's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain other matters that we have reported to management of the Village of Sterling in a separate letter dated August 27, 2008.

View of Responsible Officials and Planned Corrective Actions:

Financial Statement Preparation

The Village has evaluated the cost vs. benefit of establishing internal controls over the preparation of financial statements in accordance with GAAP, and determined that it is in the best interests of the Village to outsource this task to its external auditors, and to carefully review the draft financial statements and notes prior to approving them and accepting responsibility for their content and presentation.

Separation of Duties in the Performance of Functions

The Village Clerk and Treasurer will review their current duties and analyze possible areas for changes in functions performed by specific individuals in order to strengthen internal control.

General Ledger Activity

The Village Clerk will review the general ledger activity periodically to check for accuracy, and will reclassify expenditures and revenues to the correct general ledger accounts as needed.

Bank Accounts

The Village Treasurer will review the outstanding items on the bank reconciliations and will remove the items that have previously cleared the bank. The Treasurer will continue to reconcile the bank accounts on a monthly basis. In addition, the Treasurer will take better care to review the outstanding items and reconcile the cash balances per the computer system on a monthly basis.

Unrecorded Assets

The Village will record all assets in the general ledger system as of the date they are obtained and will seek guidance if necessary to create the proper general ledger account.

Village Board Reports

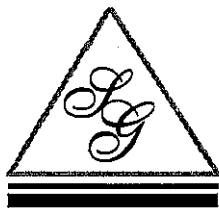
The Village Clerk will develop and present financial reports to the Village Council on at least a quarterly basis. These reports will be produced from the current financial software package based on the reconciled general ledger activity.

The Village of Sterling's responses to the findings identified in our audit are described above. We did not audit the Village of Sterling's responses and, accordingly, we express no opinion on them.

Members of the Village Council
Village of Sterling
August 27, 2008

This report is intended solely for the information and use of management, the Members of the Village Council, and the State of Michigan and is not intended to be and should not be used by anyone other than these specified parties.

Stephenson, Grault & Co., P.C.



Stephenson, Gracik & Co., P.C.

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Herman A. Bertuleit, CPA

August 27, 2008

Members of the Village Council
Village of Sterling
Arenac County, Michigan

Dear Council Members:

We have audited the financial statements of the governmental activities, the business-type activities, and each major fund of the Village of Sterling for the year ended March 31, 2008, and have issued our report thereon dated August 27, 2008. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under U.S. Generally Accepted Auditing Standards and Government Auditing Standards

As stated in our engagement letter dated January 31, 2006, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of the Village of Sterling. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Village of Sterling's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter dated January 31, 2006 and in our meeting about planning matters on July 23, 2008.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Village of Sterling are described in Note 1 to the financial statements. As described in Note 2, the Village of Sterling has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, as of March 31, 2008. We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

Members of the Village Council
Village of Sterling
August 27, 2008
Page 2

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. The audit adjustments, which include material misstatements detected as a result of audit procedures, were provided to and corrected by management.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated August 27, 2008.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

In planning and performing our audit of the financial statements of the Village of Sterling for the year ended March 31, 2008, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. As a result of our consideration of the internal controls and tests of compliance as described in the third and fourth paragraphs, we offer the following recommendations for consideration.

Financial Statement Preparation

The Village of Sterling prepares various financial information throughout the year to assess operations and the financial condition of the Village. However, prior to the closing of the year end, various entries material to the financial statements were proposed by our firm. Also, the Village relies on our firm to assist in preparing the annual financial report in accordance with Generally Accepted Accounting Principles.

The Village of Sterling has individuals on staff to review that the financial report is accurate and the financial information reflects the recording of the proposed entries, however, not to review and determine that the financial report is a complete presentation in accordance with Generally Accepted Accounting Principles. As a result, the Village is considered to have a significant control deficiency, since reporting errors or omissions could occur in the preparation of the annual financial report that would be departures from Generally Accepted Accounting Principles and the Village would not be in a position to detect the errors or omissions.

Separation of Duties in the Performance of Functions

The present system of internal accounting controls does not provide for separation of duties in the performance of functions. In our opinion, the system is adequate to account for the financial activity of the Village of Sterling but could be strengthened by a few minor changes in the personnel assigned to perform certain functions.

We recommend that the cash receipts and cash disbursements functions be handled by different individuals. Cash receiving should be centralized in a person without authority to sign checks and without access to noncash accounting records and not involved in reconciling bank accounts. A different person should prepare checks and reconcile the bank accounts.

General Ledger Activity

During our fieldwork, we again noted various improper postings of receipts and disbursements and inconsistent treatment of revenue and expense transactions. We also noted that the Village did not record all of the receivables in the general ledger. We recommend that the Village post receipts and disbursements to the proper accounts in accordance with the State chart of accounts. We also recommend that the Village record all receivables in the general ledger system at the time that the billings are generated.

Bank Accounts

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Unrecorded Assets

During our fieldwork it was brought to our attention that the Village opened a new bank account in the current year that was not recorded in the general ledger. This activity was recorded through audit adjustments. After the audit was complete, the Village obtained the necessary guidance to record the account properly in the general ledger. We recommend that the Village record all assets in the general ledger system as of the date they are obtained.

Members of the Village Council
Village of Sterling
August 27, 2008
Page 4

Village Board Reports

The Village Council was not provided with quarterly financial and budget reports as required by the State of Michigan Accounting Manual. As a result the Village did not monitor it's budget during the year. We recommend that the Village Clerk provide at least quarterly reports to the Village Council, for each fund, that include a balance sheet and profit and loss statements with a budget to actual presentation. These reports will be useful in controlling the budget as well as making other necessary financial decisions.

Deficit Fund Balance

The Village's Local Street Fund has a deficit fund balance at March 31, 2008. We also noted that the Village budgeted for the Local Street Fund to have total estimated expenditures in excess of total estimated revenues for year ended March 31, 2008. A deficit elimination plan was filed with the Michigan Department of Treasury after the March 31, 2007 fiscal year end that eliminates the deficit within five years.

Budget Control

We noted that the Village's General Fund included expenditures in various activities that exceeded appropriated amounts. We recommend that the Village Council amend the budgets for all funds periodically as needed and take into consideration recurring year end audit adjustments.

We wish to express our appreciation for the cooperation and courtesies extended our staff by management and employees of Village of Sterling.

This information is intended solely for the use of management, the Members of the Village Council, and the State of Michigan and is not intended to be and should not be used by anyone other than these specified parties.

Stephenson, Grainh & Co., P.C.